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Supreme Court of the United States

No. 863 October Term, 1940.

THE CITY OF NEW YORK,
Petitioner,

against

MICHAEL FRIEDEL, Trustee in Bankruptcy of NATIONAL STUDIOS, INC.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

Whether upon the bankruptcy of a retailer who has, or should have, collected sales taxes from customers and who should have forwarded them to the Comptroller of the City of New York, the sums found owing by the bankrupt are owed to the City qua debt or qua tax. City contends that New York Court of Appeals has held that they are owed qua tax, and that contrary holding of majority of Court below is highly prejudicial to its efforts to secure revenues with which to meet emergency. Under similar state laws, opposite result was reached in Tenth Circuit and in Courts of last resort of other States. Construction of 1938 Amendments to National Bankruptcy Act.

March 21, 1941.

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THE CITY OF NEW YORK,
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MICHAEL FEHRING, Trustee in Bankruptcy of
NATIONAL STUDIOS, INC.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

To the Honorable the Supreme Court of the United States:

The petition of the City of New York respectfully shows:

1. Your petitioner is a municipal corporation organized and existing under and by virtue of the laws of the State of New York.

2. In a certain proceeding in bankruptcy in the United States District Court for the Southern District of New York, commenced in 1939 and known as *In re National Studios, Inc.*, claims were duly filed by your petitioner, and also by other claimants whose interests are not presently relevant. The respondent is the trustee in bankruptcy of National Studios, Inc., and the custodian of such assets as are available for the payment of creditors.

3. The bankrupt sold certain goods at retail to its customers, and was required by the New York City Sales Tax Local Law (Local Law No. 24 of 1934, as amended and con-

tinued by divers local laws annually passed—the text of the law being printed in the Appendix, *post*, p. 25) to collect from its customers a 2% sales tax on each purchase.

4. The sum originally demanded as sales taxes which the bankrupt should have collected from its customers was reduced by compromise, and by stipulation at the hearing (R., 12), to $796. Of this sum the bankrupt had collected $60 only from its customers, and even this sum had not been segregated and could not be traced into the possession of the trustee (R., 12).

5. The National Bankruptcy Act, § 64, as amended by 52 Stat. 840, 874, awards priority in bankruptcy to "taxes legally due and owing by the bankrupt to the United States or any State or any subdivision thereof * * *." A provision formerly forming part of this section and awarding priority (after taxes) to "debts owing to any person who by the laws of the States or the United States is entitled to priority" was modified by striking out the words "the States or," so that it possesses no present pertinence.

6. The referee in bankruptcy held that the City's claim against a retailer, such as the bankrupt was, for sums of money which were or ought to have been collected by way of sales taxes from its customers, was a claim for taxes. The sums which the bankrupt owed, he held, were owed *qua* tax and not *qua* debt. He allowed the claim priority.

7. The District Court reversed the referee and said the sums owed were owed *qua* debt and not *qua* tax.

8. The Circuit Court of Appeals affirmed the District Court, CHASE, J., with whom SWAN, J., concurred writing the prevailing opinion. CHARLES E. CLARK, J., wrote a dissenting opinion. The decision was handed down on March 17, 1941.

Jurisdiction and Timeliness.

9. The petition is made under U. S. Code, tit. 28, § 347, subd. (a), and the Court has jurisdiction to grant the writ. *New York City* v. *Goldstein, Trustee in Bankruptcy,* 299 U. S. 522 (1937).

10. Since the decision of the Circuit Court of Appeals was handed down on March 17, 1941, the order of affirmance being entered March 19, 1941, the petition is timely.

11. The record remains in the custody of the Clerk of the United States Circuit Court of Appeals. The mandate issued forthwith, Rule 30 of the Rules of the Circuit Court of Appeals, Second Circuit, being waived by stipulation.

Statutes Involved.

12. The City Sales Tax Local Law is printed in the Appendix, *post,* p. 25. We show in the subjoined brief our reasons why we say this local law impresses upon the obligation of the bankrupt retailer the characteristics of a *tax* rather than a *debt.*

13. The pertinent portion of the National Bankruptcy Act will be found in Par. 5, *supra.*

Opinions Below.

14. Four opinions merit the attention of this Court, *viz.,* that of the Referee, that of the District Court, that of the majority of the Circuit Court of Appeals, and that of the dissenting Judge.

(i)

The Referee stated that the case presented to him in the City's proof of claim and the Trustee's objections there-

to required him "to determine whether the claim of the City of New York is a claim for a tax legally due and owing by the bankrupt or whether it is a claim against the bankrupt only as a collector of such taxes" (R., 14). He then adverted to the requirement in the local law that every vendor is to "file with the comptroller a return of his receipts and of the taxes payable thereon" (§ 5, R., 14, 15); thereafter quoted the first paragraph of § 8, set forth *post*, p. 27; and finally cited the right to order the sheriff to make a distraint, also set forth *post*, p. 28. He concluded (R., 15):

> "These provisions of the law impose two liabilities upon the vendor: one is to collect the tax from the vendee and pay it to the City; the other liability is to pay the City the amount of the tax whether the vendor collects it or not. This latter obligation is a tax legally due and owing by the bankrupt. Such was the reasoning of the Court in *Matter of Atlas Television Co., Inc.*, 273 N. Y. 51, and since the claim of the City of New York expressly claims that the bankrupt is justly and truly indebted to it for taxes the claim is entitled to priority."

(ii)

The District Judge cited (R., 23-24) three decisions of the New York Court of Appeals on the nature of the seller's obligations under the sales tax local laws: *Matter of Atlas Television Co.*, 273 N. Y. 51 (1936); *Matter of Merchants Refrigeration Co.* v. *Taylor*, 275 N. Y. 113, 124 (1937); and *Matter of Kesbec, Inc.* v. *McGoldrick*, 278 N. Y. 293, 297 (1938). From these he concluded that the sales tax local law imposes a duty on the vendor to forward collections to the City but does not impose the burden of the tax *qua* tax upon him. He also cited *McGoldrick* v. *Berwind-White Coal Mining Co.*, 309 U. S. 33 (1940), as holding the tax was on the purchaser since it was held not to burden a seller engaged

in interstate commerce.* He concluded that when the decision of this Court in *Matter of Lazaroff*, 84 F. (2d) 932 (2nd Circ., 1936), was reversed *sub nom. New York City* v. *Goldstein*, 299 U. S. 522 (1937), upon the authority of *Matter of Atlas Television Co., supra*, this Court upheld the City's asserted priority because the bankrupt owed a debt to the City under the National Bankruptcy Act, U. S. Code, tit. 11, § 104(7) and did not owe a tax under § 104(6); so that the amendment of 1938 (52 Stat. 874) stripping debts owing to cities of any right to priority compels the City to show that vendors owe sales taxes (collected or collectible from their customers) *qua* taxes and not *qua* debts. This, he said, the City cannot do. He accordingly reversed the Referee.

(iii)

Judge CHASE, with whom Judge SWAN concurred, held that when *Matter of Atlas Television Co.*, 273 N. Y. 51 (1936), was decided, the City had priority under state law regardless of whether its claim against a retailer was a claim for a tax or a claim for a debt. The Circuit Court of Appeals had, prior to that decision, held that such a claim was one for a debt. *Matter of Lazaroff*, 84 F. (2d) 982 (2nd Circ., 1936). This Court reversed that decision on the authority of the *Atlas* case, *sub nom. New York City* v. *Goldstein*, 299 U. S. 522 (1937). But this Court, said Judge CHASE, did not disapprove of so much of the *Lazaroff* opinion as held the claim to be a debt and not a tax, since the City, under the National Bankruptcy Act as it then stood, was entitled to prevail whichever way the claim was categorized. This was error, as we show *post*, p. 20. The

* As we show *post*, p. 19, we are not in any sense going back on the position we took at the bar of this Court in the *Bernind-White* case.

Court, therefore, renewed and reiterated the declarations it had made in *Matter of Lazaroff, supra,* as well as in *Nolte* v. *Hudson Navigation Co.,* 8 F. (2d) 859 (2nd Circ., 1925), that sums owed by retailers, for taxes collected of collectible from their customers, are owed *qua* debt and not *qua* tax.*

(iv)

Judge CLARK dissented, and pointed out that in the *Atlas* opinion the New York Court of Appeals had expressly criticized the *Lazaroff* opinion as reflecting an erroneous interpretation of New York law, and as denominating a *debt* what was really, in the judgment of the New York Court of Appeals, a *tax.*

Judge CLARK also referred to a holding in the Tenth Circuit that what the retailer owes in circumstances like those at bar is owed *qua* tax and not *qua* debt. *Barbee, Trustee* v. *Oklahoma Tax Commission,* 103 F. (2d) 114 (10th Circ., 1939). Two law review notes to the same effect (18 N. Y. Univ. Law Q. Rev. 135; 40 Columbia L. Rev. 1241) were also cited.

Summary Statement of the Matter Involved.

15. The question is whether, when the taxing authorities have imposed, by law, a sales tax designed to rest upon

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* This narrow view of the effect to be given to this Court's reversal of the *Lazaroff* decision is at variance with the view generally entertained by federal district Judges in the Eastern and Southern Districts of New York. Prior to the amendment of the National Bankruptcy Act, § 64, district Judges had no hesitancy in describing the claim of the City of New York against retail merchants for sums collected from their customers as claims for *taxes* owing by the retailers. See for example *In re Sixty-seven Wall Street Corporation,* 23 F. Supp. 672 (S. D. N. Y., 1938). It is also true that Referees in bankruptcy (including the Referee in the case at bar) likewise shared the view of the district Judges.

consumers, but have required retailers to collect and hand over the taxes, the retailers owe what they have or should have collected, *qua* tax or *qua* debt. Under § 64 of the National Bankruptcy Act as amended (52 Stat. 874), the City is preferred if the sums are owed *qua* tax but not if they are owed *qua* debt. We contend that (1) since the retailers are required to file returns, (2) since they are liable for the amount of the tax whether they have actually collected it from their customers or not, (3) since upon a failure to collect and pay over the sales tax they may be proceeded against by distraint, and (4) since sales taxes cannot be effectively collected in any other way save by having them funnelled through retailers, the decision below was erroneous and prejudicial to the public interest. And it is certainly irreconcilable with *Matter of Atlas Television Co.*, 273 N. Y. 51 (1936), discussed in the subjoined brief.

Questions Presented.

16. The questions presented are:

1. When a sales tax law requires retailers to collect sales taxes from customers and forward the collections to the taxing authorities, and requires retailers to file periodic returns, and subjects them to drastic measures upon non-fulfillment of their duties, and makes them liable for the amount of the tax whether they have collected it from their customers or not, are the sums collected or collectible by retailers owed to the taxing authorities *qua* debt or *qua* tax?

2. Was the Circuit Court of Appeals warranted in rejecting the authority of decisions of the New York Courts defining the retailer's obligation in the premises as a tax?

3. If the Circuit Court of Appeals did admit that state decisions were controlling, did it correctly interpret them?

4. Should not the conflict between the Second Circuit and the Tenth Circuit (see *Barbee, Trustee* v. *Oklahoma Tax Commission*, 103 F. [2d] 114 [1939]) be resolved by a declaration that the Tenth Circuit was correct?

5. Should not the phrase "taxes legally due and owing * * * to * * * any State or any subdivision thereof," in National Bankruptcy Act § 64, as amended in 1938, be construed to cover the obligations of the bankrupt at bar to the City of New York?

Assignment of Errors.

17. Your petitioner submits that the Court below erred in holding that what the retailer owed in the premises was owed *qua* debt and not *qua* tax; erred in that it either rejected or misconstrued the applicable decisions of the New York Court of Appeals; erred in misconstruing *New York City* v. *Goldstein*, 299 U. S. 522 (1937); and erred in rejecting the reasoning which led to an opposite result in *Barbee, Trustee* v. *Oklahoma Tax Commission, supra.*

Reasons for Allowance of Writ.

18. Sales taxes as an emergency revenue measure have been imposed by legislation in 20 States.* The amount of a sales tax is, in a majority of the transactions taxed, mea-

* The trend away from *ad valorem* taxes, as sources of state revenue, to other kinds of taxes has been recognized by this Court. *Superior Bath House Co.* v. *McCarroll*, 312 U. S. . . . , 61 Sup. Ct. 503, 505 (Feb. 3, 1941, Cal. No. 180).

sured in pennies. To proceed against the purchaser and to require him to make a return is impracticable, and would cost in administration more than the taxes would bring in in revenue. Sales taxes can only be efficiently collected if they are funnelled through retailers, and obligations of a drastic character imposed upon them. Cf. JACOBY, *Retail Sales Taxation* (1938), p. 100. The local law at bar follows this course. To construe the local law in such a way as to reduce the retailer's obligation from an obligation to pay a *tax* to a mere duty to pay a *debt*, with the consequence that the taxing authorities are deprived of a preference in bankruptcy, is to impose a very serious obstacle in the way of tax collections, and to bring about a very serious diminution of state and municipal revenues. The taxes were imposed to meet an emergency. The local authorities have decided to renew the tax annually on the ground that the emergency has not passed.* The decision below contravenes the public interest so patently as to merit review here.

19. Public importance attaches to the question by reason of the further circumstance that the question is presented in no less than 1,000 bankruptcies in which the City of New York has appeared as a claimant with a claim for sales taxes.

20. The decision below also tends to contravene the nearest applicable decisions in the highest Court of the State and in this Court.

21. The precise question has never been passed upon in this Court since the amendment to the National Bankruptcy Act made in 1938, and in view of the widespread vogue of sales taxes, the writ should issue.

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* Proof that an emergency still exists in New York is found in the titles of two Acts signed by Governor LEHMAN on March 20, 1941. New York Laws of 1941, ch. 135 and ch. 137.

WHEREFORE, your petitioner prays that a writ of certiorari may be issued out of and under the seal of this Court, directed to the United States Circuit Court of Appeals for the Second Circuit, commanding the said Court to certify and send to this Court, on a day certain to be therein designated, a full and complete transcript of the record and all proceedings of the said Circuit Court of Appeals for the Second Circuit in this case, being No. 171 on its calendar for the October Term, 1940, to the end that the case may be reviewed and determined in this Court, as provided in Title 28, § 347 of the Code of Laws of the United States, and that the said final order of the said Circuit Court of Appeals for the Second Circuit in this case, and every part thereof, may be reviewed by this Court, and the determination of the said Circuit Court of Appeals for the Second Circuit, as well as the determination of the United States District Court for the Southern District of New York, which was affirmed by the said United States Circuit Court of Appeals for the Second Circuit, may be reversed and a mandate issued directing the allowance of the asserted priority; and your petitioner prays for such other and further relief as to this Court shall seem just and equitable; and your petitioner will ever pray.

New York, N. Y., March 21, 1941.

THE CITY OF NEW YORK,
Petitioner,

By WILLIAM C. CHANLER,
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City of New York,
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Supreme Court of the United States

No. . October Term, 1940.

THE CITY OF NEW YORK,
Petitioner,

against

MICHAEL FEIRING, Trustee in Bankruptcy of NATIONAL STUDIOS, INC.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI.

The case involves an important question under the 1938 amendment to the National Bankruptcy Act. In its claim to priority, on the ground that sales taxes collected or collectible from customers and not paid over to the authorities by the retailer when his bankruptcy intervened were owed *qua* tax and not *qua* debt, the City was successful before the Referee, but unsuccessful before the District Court and the Circuit Court of Appeals. A strong dissenting opinion, however, was written by Judge CHARLES E. CLARK.

POINT I.

The terms of the local laws under which the sales taxes were imposed, and the interpretation of them by the New York Court of Appeals, stamp upon the retailer's obligations the characteristics of a tax as distinguished from a mere debt. Priority in bankruptcy should have been awarded, as it was under substantially similar circumstances in the Tenth Circuit.

1. Features of local law relied on.

Local Law No. 20 of 1934 (erroneously numbered "21" in the compilation published at Albany), as amended by

Local Law No. 24 of 1934 (erroneously numbered "25" in the cited compilation), imposes (in § 2) a tax upon "receipts from every sale in the city of New York" of "tangible personal property sold at retail", with exceptions not here relevant.*

Section 2 goes on to provide:

> "Upon each taxable sale or service the tax to be collected shall be stated and charged separately from the sale price or charge for service and shown separately on any record thereof, at the time when the sale is made or evidence of sale issued or employed by the vendor and shall be paid by the purchaser to the vendor, for and on account of the city of New York, and the vendor shall be liable for the collection or the service rendered; and the vendor shall have the same right in respect to collecting the tax from the purchaser, or in respect to non-payment of the tax by the purchaser, as if the tax were a part of the purchase price of the property or service and payable at the time of the sale."

Section 5 requires every vendor to "file with the comptroller a return of his receipts and of the taxes payable thereon" for various prescribed periods. The section also contains these words:

> "If he deems it necessary in order to insure the payment of the tax imposed by this local law the comptroller may require returns of receipts to be made for other than the aforesaid periods and upon such dates as he may specify."

Section 6 contains provisions in reference to security to be furnished by the vendor "to secure the payment of any

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* Both of these local laws, and the ensuing local laws continuing the taxes for later years, were passed under a special Enabling Act (New York Laws of 1934, ch. 873) to raise revenue for the relief of unemployment.

tax and/or penalties due or which may become due from such vendor". We quote the section in full:

> "§ 6. **Payment of taxes.** At the time of filing a return of receipts each vendor shall pay to the comptroller the taxes imposed by this local law upon the receipts required to be included in such return. *All taxes for the period for which a return is required to be filed shall be due from the vendor* and payable to the comptroller on the date limited for the filing of the return for such period, without regard to whether a return is filed or whether the return which is filed correctly shows the amount of receipts and the taxes due thereon. The comptroller may require any vendor required to collect the tax imposed by this local law to file with him a bond, issued by a surety company authorized to transact business in this state and approved by the superintendent of insurance of this state as to solvency and responsibility, in such amount as the comptroller may fix, to *secure the payment of any tax* and/or penalties due or which may become *due from such vendor.* In lieu of such bond, securities approved by the comptroller, in such amount as he may prescribe, may be deposited with him, which securities shall be kept in the custody of the comptroller and may be sold by him at public or private sale, without notice to the depositor thereof, if it becomes necessary so to do in order to *recover any tax* and/or penalties due. Upon such sale, the surplus, if any, above the amounts due under this local law shall be returned to the person who deposited the securities." (Italics ours.)

Sections 7 and 10 provide the vendor with the remedy of certiorari where an erroneous determination of the tax is alleged to have been made by the Comptroller, or where a tax has been illegally collected and the Comptroller has failed to make a refund to the vendor. Section 7 gives drastic remedies against a vendor who has failed to file a

return, even allowing the Comptroller to estimate the amount owed "on the basis of external indices, such as number of employees of the person concerned, rentals paid by him, his stock on hand, and/or other factors"—surely a harsh way of treating a mere "debtor".

Further remedies against the vendor are given by § 8, which reads in part as follows:

> "§ 8. **Proceeding to recover tax.** Whenever any vendor or purchaser shall fail to collect and pay over *any tax and/or to pay any tax* or penalty imposed by this local law as in this local law provided, the corporation counsel shall, upon the request of the comptroller, bring an action to enforce the payment of the same.
>
> As an additional or alternate remedy, the comptroller may issue a warrant, directed to the sheriff of any county within the city of New York, commanding him to levy upon and sell the real and personal property of the vendor or purchaser which may be found within his county, for the payment of the amount thereof, with any penalties, and the cost of executing the warrant, and to return such warrant to the comptroller and to pay to him the money collected by virtue thereof within sixty days after the receipt of such warrant. The sheriff shall within five days after the receipt of the warrant file with the clerk of his county a copy thereof, and thereupon such clerk shall enter in the judgment docket the name of the person mentioned in the warrant and the *amount of the tax* and penalties for which the warrant is issued and the date when such copy is filed. Thereupon the amount of such warrant so docketed shall become a lien upon the title to and interest in real property and chattels real of the person against whom the warrant is issued in the same manner as a judgment duly docketed in the office of such clerk. The sheriff shall then proceed upon the warrant in the same manner, and with like effect, as that pro-

vided by law in respect to executions issued against property upon judgments of a court of record, and for services in executing the warrant he shall be entitled to the same fees, which he may collect in the same manner." (Italics ours.)

The vendor's obligation is measured either by the size of his tax collections or by 2% of his receipts from sales, whichever is greater.* His obligation is owed *qua* tax.

Moreover, where the price is below a certain figure, the Comptroller is empowered (§ 3, last sentence) to excuse the vendor from the duty of collecting from the purchaser. The figure was fixed at $0.12 by the Comptroller's Regulations of February 11, 1935, Art. 3. The result of this has been held to be that, on sales below this figure, the vendor is primarily and solely liable. *Queens Vending Corp.* v. *City of New York,* 94 N. Y. L. J. 318 (July 31, 1935), aff'd 246 App. Div. 594 (1st Dept., 1935). A similar result under a somewhat similar statute was reached in *Jensen Candy Co.* v. *State Tax Commission,* 90 Utah 359, 61 Pac. (2d) 629 (1936).

2. The New York Court of Appeals has declared that what the retailer owes is owed *qua* tax. It has expressly disapproved the contrary ruling by the Circuit Court of Appeals in the *Lazaroff* case.

In *Matter of Atlas Television Co.,* 273 N. Y. 51 (1936), the "city of New York filed a claim for 'taxes imposed pursuant to the provisions of Local Law No. 24 of the City of New York for the year 1934' " (p. 53). In describing

* Comptroller's Regulations, issue of December 29, 1938, p. 31.

how the Courts below had viewed our claim, the Court of Appeals said (p. 55):

> "The courts below, too, have assumed that the city has such a preference in the collection of taxes. Preference has been denied in this case because in the opinion of the Appellate Division the city's claim is not for taxes due to the city from the insolvent, but for moneys collected by the insolvent as agent for the city."

The Court used similar language in describing the arguments which the assignee in that case had interposed against ours, saying (pp. 55-56):

> "It is the contention of the assignee that even though the vendor of property is the person entitled to the 'receipts from every sale,' the tax is laid upon the purchaser, and that the vendor is required only to collect the tax as the collecting agent of the city and though required to pay to the city the amount of the tax, his liability is only that of an ordinary debtor."

The Court then gave a synopsis of the holding in *Matter of Lazaroff*, 84 F. (2d) 982 (2nd Circ., 1936), and said (p. 57):

> "We might agree with that conclusion if the local law did not contain other provisions which indicate that the obligation imposed upon the vendor is in the nature of a tax. He must file a return of his receipts from sales. (§ 5.) The duty of payment *to the city* is laid upon the vendor, not the purchaser. His liability is not measured by the amount actually collected from the purchaser but by the receipts required to be included in such return. (§ 6.) He must pay the tax even if failure to collect is due to no fault of his own. Indeed the city has insisted that a vendor is liable for a tax of two per cent upon the amount of his receipts even from sales within the amount, stated in regulations promulgated by the Comptroller

> pursuant to section 3 of the local law, upon which 'no tax need be collected from the purchaser.' (*Queens Vending Corp.* v. *City of New York*, 246 App. Div. 594)."

To ignore this paragraph, as the majority below did, was a clear disregard of an applicable decision of the state Court of last resort. The dissenting Judge pointed this out.

The Court then proceeded to hold that taxation was an attribute of sovereignty and that the City acted as sovereign when it imposed taxes for governmental purposes (p. 57). The Court concluded (pp. 57-58):

> "From that point of view it seems clear that the city is entitled to a priority. It has imposed a tax as sovereign and to meet a need which concerns the welfare of the State. It has provided that the vendor of property must pay the tax to it. Though the vendor is required, at least in most cases, to collect the tax from the purchaser 'for and on account of the city,' the purpose of that provision is to place the incidence of the tax immediately on the consumer. The city can collect only from the vendor. The vendor's obligation to pay the tax is not measured by the amount collected nor dependent upon failure to exercise the diligence in collection which would be required of an agent. It is an obligation measured by the receipts of the vendor and created by the local law."

We submit that nothing could be more firmly and dogmatically declared than that the City may demand the tax of the vendor *qua* tax.

Judge LEHMAN, in the *Atlas Television* case, having said that "the purpose of that provision * is to place the inci-

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* The provision requiring the vendor to collect the tax from the purchaser.

dence of the tax immediately on the consumer" (p. 58), the statement of CRANE, Ch.J., in *Matter of Merchants Refrigeration Corp.* v. *Taylor*, 275 N. Y. 113, 124 (1937), to wit:

> "The *Atlas Television* case (273 N. Y. 51) did not hold that the sales tax is imposed on the vendor, but only that he is under a duty to pay the tax to the city regardless of whether or not the vendor collects it from the purchaser",

must refer to the ultimate incidence of the burden of the tax, and does not diminish the duties and obligations of the vendor *vis-à-vis* the City, which are to pay over 2% of his receipts, *qua* tax and not *qua* debt. And we say the same thing of Judge LOUGHRAN'S opinion in *Matter of Kesbec, Inc.* v. *McGoldrick*, 278 N. Y. 293 (1938), where he said (p. 297):

> "The sales tax was not imposed on the vendor. It fell upon the purchaser * * * *"*

citing the *Merchants Refrigeration* opinion. He, too, like Chief Judge CRANE before him, meant that when all the duties imposed by the Sales Tax Local Law have been performed, it is the purchaser whose pocketbook has been hit, and that in consequence the vendor had no right to keep sums collected in excess of what the law required. But none the less, what the vendor owes he owes *qua* tax. The dissenting Judge (CLARK, J.) agreed with us that the later decisions do not impair the authority of the *Atlas* case.

All doubts on this score would seem to have been set at rest by the very recent decision in the Court of Appeals in *Matter of David Brown Printing Co., Inc.*, 285 N. Y. _____ (March 6, 1941), wherein upon the insolvency of a retailer, the Court of Appeals unanimously declared that the claim of the City of New York for sales taxes should share equally with a claim by the State of New York for a franchise tax,

thus reiterating in strong terms their view that the obligation of a retailer was an obligation to pay a *tax* and not merely an obligation to discharge a *debt*.

The vendor has the duty of passing the burden on to the purchaser, but again we say that what the vendor pays to the City he pays *qua* tax because (1) "the amount due to the City is not measured by the amount actually collected from the purchaser, but by a percentage of the vendor's total receipts;" * and (2) the reenforcement of the City's right by the requirement that periodic returns be filed by the vendor as well as by the reservation of a right of distraint takes away from the vendor's liability the attributes of a debt and confers upon it the attributes of a tax.† Above all, it is certainly anomalous to classify as a debt and not a tax an obligation into the assumption of which the vendor's volition did not enter at all.

McGoldrick v. *Berwind-White Coal Mining Co.*, 309 U. S. 33, 43-44 (1940), established nothing hostile to the foregoing. The tax was sustained against an assertion that it burdened interstate commerce, for the simple reason that the seller enjoyed a right, and in fact was under a duty, to pass on the tax to the purchaser. This does not mean that what the seller collected, in fruition of that right or in performance of that duty to shift the incidence, was any the less a tax and owing to the authorities as such. The use the trustee made below of the *Berwind-White* case seems to us to

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* 18 N. Y. Univ. L. Q. Rev. 136, lines 3-4.

† The capacity of "reenforcements" to change the character of an obligation was adverted to in *McDowell* v. *City of Barberton*, 38 F. (2d) 786 (6th Circ., 1930), where the Court said (p. 788): "But the state gave the color and standing of taxes to municipal water rents to the extent at least that it secured their collection by a possible lien upon the real estate, and we think this peculiarity should be recognized by section 64(a) of the Bankruptcy Act (11 U. S. C. A., § 104(a))."

See also *In re Otto F. Lange Co.*, 159 Fed. 586, 588 (N. D. Iowa, 1908).

involve a transgression of the principle, first uttered in *Cohens* v. *Virginia*, 6 Wheat. 264 (1821), that "general expressions, in every opinion, are to be taken in connection with the case in which the expressions are used" (p. 399).

Another reason why the true holding of the *Atlas Television* case must have been what we have stated above is that while the State of New York under state law enjoys priority whether it seeks to enforce a debt or a tax, municipalities under state law enjoy priority only when they are seeking to collect taxes. The sovereignty of the State, and the privileges appurtenant to sovereignty, are shared with municipalities as far as taxes are concerned but not as far as debts are concerned. See *Matter of Northern Bank of New York*, 85 Misc. 594 (1914), aff'd on opinion below 162 App. Div. 974 (1st Dept., 1914), aff'd 212 N. Y. 608 (1914). Here the City, having collected various local taxes, deposited them in a bank which later failed. Clearly the bank owed the money to its depositor *qua* debts and not *qua* taxes. Priority was, under those circumstances, denied.

3. To grant the City the claimed priority would not contravene anything said by this Court in *New Jersey* v. *Anderson*.

We are not unmindful of the statement in *New Jersey* v. *Anderson*, 203 U. S. 483, 491 (1906) that a State "cannot conclusively decide that to be a tax within the meaning of a Federal law, providing for the payment of taxes, which is not so in fact". But that language, in actual practice, seems to have been treated as merely a *caveat* against preposterous and unrealistic definitions; and a recent commentator has said (40 Columbia L. Rev. 1243):

> "Despite this declaration that the federal courts are to make the ultimate decision, the courts have fol-

lowed almost without question the interpretations of the state courts and the language of the state statutes. No bankruptcy case has been found in which a federal court has disagreed with the terminology applied to a particular levy by a state court or disregarded the terms in which the state legislature describes the exaction."

Surely had this Court been disposed to feel any doubt as to the reasonableness of the *Atlas* decision and its capacity to bind federal Courts sitting in New York, it would not have pursued the extraordinary course of reversing the Circuit Court of Appeals *ex parte* without argument, as it did in *New York City* v. *Goldstein, supra.*

4. A conflict among the Circuits is presented.

Upon facts strikingly similar to those at bar, priority was allowed to a state tax commission upon the bankruptcy of a vendor, in *Barbee, Trustee* v. *Oklahoma Tax Commission,* 103 F. (2d) 114 (10th Circ., 1939). The sales tax law of Oklahoma, Okla. L. 1935, ch. 66, p. 311, provided:

> "The tax levied hereunder shall be paid by the consumer and/or user to the vendor, and it shall be the duty of each and every vendor in this State to collect from the consumer or user, the full amount of the tax imposed by this Act, or an amount equal as nearly as possible and/or practicable to the average equivalent thereof.
>
> Vendors shall add the tax imposed under this Act, or the average equivalent thereof, to the sales price or charge, and when added such tax shall constitute a part of such price or charge, shall be a debt from consumer or user to vendor until paid, and shall be recoverable at law in the same manner as other debts."

The District Court awarded priority (23 F. Supp. 995), and the Circuit Court of Appeals affirmed, citing and fol-

lowing an Oklahoma decision, *In re Harris,* 184 Okla. 459, 88 Pac. (2d) 372 (1939), where the Court had said (p. 462):

> " * * * we conclude that the moneys due from the insolvent debtor are taxes and not merely an ordinary debt owing from him as agent to the state of Oklahoma as principal." *

POINT II.

The City having imposed the sales taxes to meet an emergency, and the Chandler Act, which *inter alia* amended the National Bankruptcy Act to read as it now does, having itself had among its objects the relief of financially embarrassed municipalities, the question of priority should be resolved in favor of the claimant City.

In 1934, Congress tried to come to the relief of municipalities by enabling them to file petitions in bankruptcy. Act of May 24, 1934, 48 Stat. 708. The statute was, to be sure, held unconstitutional in *Ashton* v. *Cameron County Water Improvement District,* 298 U. S. 513 (1936). As amended by the Act of August 16, 1937, 50 Stat. 653, however, the legislation was upheld. *United States* v. *Bekins,* 304 U. S. 27 (April 25, 1938).

It would convict the members of Congress of singular ineptitude if, after having exhibited such persistence in their effort to relieve municipalities, they were deemed (in the Act of June 22, 1938, 52 Stat. 874, passed less than two months after success had crowned their efforts) to have placed municipalities under the handicap of enjoying a less extensive priority in enforcing tax claims in bankruptcy than had previously been theirs. A holding that *New York*

* The Supreme Court of Oklahoma cited and followed *Matter of Atlas Television Co., supra,* and *Matter of Rockaway Paint Centre,* 249 App. Div. 66 (2nd Dept., 1936).

City v. *Goldstein*, 299 U. S. 522 (1937), has ceased to be authoritative since the passage of the Act of June 22, 1938, is therefore, a result to be avoided.

The debates, moreover, also implement what we have just stated. Congress in the debates on the bill which later became the Act of August 16, 1937, showed (81 Cong. Rec., part 6, p. 6313) an awareness of the impotence of the taxing power of the average municipality to afford adequate relief in times of emergency. In later amending this Act by the Act of June 22, 1938 (52 Stat. 840, at p. 940), which is the very Act by which the priority section was amended (see *supra*, p. 2), they cannot have intended to effect a deliberate impairment of the already inadequate taxing power by making tax collections in bankruptcy more difficult.

We may further reenforce our argument by pointing to the circumstance that before the adoption of the 1938 amendment, legislation had been adopted not only in New York City but in approximately 20 States, providing for retail sales taxes and imposing upon vendors the duty to collect the taxes from customers and transmit them to the authorities. While judicial decisions that what a vendor owed under these circumstances he owed *qua* tax, had, prior to 1938, been handed down in only two States, *Doby* v. *State Tax Commission*, 234 Ala. 150, 153, 174 So. 233 (1937), and *Matter of Atlas Television Co.*, 273 N. Y. 51 (1936), which was followed in *New York City* v. *Goldstein*, 299 U. S. 522 (1937), yet it is not too much to say that the respective legislatures probably assumed that such would be the ultimate holding of the Courts—an assumption which has been borne out by several subsequent decisions, *e. g.*, *DeAryan* v. *Akers*, 12 Cal. (2d) 781, 87 Pac. (2d) 695 (1939), certiorari denied 308 U. S. 581 (1939); *State ex rel. Foster* v. *Miller*, 136 Ohio St. 295, 303, 25 N. E. (2d) 686 (1940); *In re Harris*, 184 Okla. 459, 462, 88 Pac. (2d) 372 (1939); *State Tax Commission* v. *Spanish Fork*, 99 Utah , 100 Pac. (2d) 575 (1940).

In *Doby* v. *State Tax Commission, supra,* the Court said (p. 153):

> "The retailer is the 'taxpayer', the person liable to the state for the tax. He is the person required to take out the license under [Ala. Acts, 1936-37, p. 125] section 3, the person required to make returns and pay the tax to the State Tax Commission under sections 5 and 6; the person required to keep records under section 8; the person on whose personal property a lien is declared as security for the tax under section 9."

In *DeAryan* v. *Akers, supra,* the Court held that the seller was the person on whom a tax obligation was imposed in spite of the fact that the statute contained a proviso to the effect that the "tax hereby imposed shall be collected by the retailer from the consumer in so far as the same can be done" (p. 784).

Conclusion.

The Petition for Certiorari should be granted.

New York, N. Y., March 21, 1941.

Respectfully submitted,

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APPENDIX.

Local Law No. 24 of 1934, §§ 3-8 (erroneously numbered "25" at page 164 of the compilation published at Albany).

"§ 3. **Collection of tax from purchaser.** The comptroller shall by regulation prescribe a method or methods and/or a schedule or schedules of the amounts to be collected from purchasers in respect to any receipt upon which a tax is imposed by this local law so as to eliminate fractions of one cent and so that the aggregate collections of taxes by a vendor shall, as far as practicable, equal two per centum of the total receipts from the sales and services of such vendor upon which a tax is imposed by this local law. Such schedule or schedules may provide that no tax need be collected from the purchaser upon receipts below a stated sum, and may be amended from time to time so as to accomplish the purposes herein set forth.

§ 4. **Records to be kept.** Every vendor shall keep records of receipts and of the tax payable thereon, in such form as the comptroller may by regulation require. Such records shall be offered for inspection and examination at any time upon demand by the comptroller or his duly authorized agent or employee and shall be preserved for a period of three years, except that the comptroller may consent to their destruction within that period or may require that they be kept longer.

§ 5. **Returns.** Every vendor shall file with the comptroller a return of his receipts and of the taxes payable thereon for the periods ending February twenty-eighth, May thirty-first, August thirty-first and December thirty-first, nineteen hundred and thirty-five. Such returns shall be filed within thirty days from the expiration of the period covered thereby. The comptroller may permit returns to be made by other periods so as to include all receipts during the period from December tenth, nineteen hundred and thirty-four, to December thirty-first, nineteen hundred and thirty-five, inclusive. If he deems it necessary in order to

insure the payment of the tax imposed by this local law the comptroller may require returns of receipts to be made for other than the aforesaid periods and upon such dates as he may specify.

The form of returns shall be prescribed by the comptroller and shall contain such information as he may deem necessary for the proper administration of this local law. The comptroller may require amended returns to be filed within twenty days after notice and to contain the information specified in the notice.

§ 6. **Payment of taxes.** At the time of filing a return of receipts each vendor shall pay to the comptroller the taxes imposed by this local law upon the receipts required to be included in such return. All taxes for the period for which a return is required to be filed shall be due from the vendor and payable to the comptroller on the date limited for the filing of the return for such period, without regard to whether a return is filed or whether the return which is filed correctly shows the amount of receipts and the taxes due thereon. The comptroller may require any vendor required to collect the tax imposed by this local law to file with him a bond, issued by a surety company authorized to transact business in this state and approved by the superintendent of insurance of this state as to solvency and responsibility, in such amount as the comptroller may fix, to secure the payment of any tax and/or penalties due or which may become due from such vendor. In lieu of such bond, securities approved by the comptroller, in such amount as he may prescribe, may be deposited with him, which securities shall be kept in the custody of the comptroller and may be sold by him at public or private sale, without notice to the depositor thereof, if it becomes necessary so to do in order to recover any tax and/or penalties due. Upon such sale, the surplus, if any, above the amounts due under this local law shall be returned to the person who deposited the securities.

§ 7. **Determination of tax by comptroller.** If a return required by this local law is not filed, or if a return when filed is incorrect or insufficient the comptroller shall deter-

mine the amount of tax due from such information as he may be able to obtain and, if necessary, may estimate the tax on the basis of external indices, such as number of employees of the person concerned, rentals paid by him, his stock on hand, and/or other factors. The comptroller shall give notice of such determination to the person liable for the collection and/or payment of the tax. Such determination shall finally and irrevocably fix the tax unless the vendor or purchaser against whom it is assessed shall be entitled to and within thirty days after the giving of notice of such determination apply to the comptroller for a hearing, or shall cause the same to be reviewed by certiorari, or unless the comptroller of his own motion shall reduce the same. If no opportunity for a hearing shall have been given to such person prior to the determination of the comptroller, such person may within thirty days after the comptroller shall give notice thereof, apply to the comptroller for a hearing. After such hearing the comptroller shall give notice of his determination to the applicant. The determination of the comptroller may be reviewed by certiorari if application is made to the comptroller therefor within thirty days after the giving of notice thereof. Whenever under this local law an order of certiorari is permitted it shall not be granted unless the amount of any tax sought to be reviewed, with penalties thereon, if any, shall be first deposited with the comptroller and an undertaking filed with the comptroller, in such amount and with such sureties as a justice of the supreme court of the state of New York shall approve, to the effect that if such order be dismissed or the tax confirmed the applicant for the writ will pay all costs and charges which may accrue in the prosecution of the certiorari proceeding.

§ 8. **Proceeding to recover tax.** Whenever any vendor or purchaser shall fail to collect and pay over any tax and/or to pay any tax or penalty imposed by this local law as in this local law provided, the corporation counsel shall, upon the request of the comptroller, bring an action to enforce the payment of the same.

As an additional or alternate remedy, the comptroller may issue a warrant, directed to the sheriff of any county within the city of New York, commanding him to levy upon and sell the real and personal property of the vendor or purchaser which may be found within his county, for the payment of the amount thereof, with any penalties, and the cost of executing the warrant, and to return such warrant to the comptroller and to pay to him the money collected by virtue thereof within sixty days after the receipt of such warrant. The sheriff shall within five days after the receipt of the warrant file with the clerk of his county a copy thereof, and thereupon such clerk shall enter in the judgment docket the name of the person mentioned in the warrant and the amount of the tax and penalties for which the warrant is issued and the date when such copy is filed. Thereupon the amount of such warrant so docketed shall become a lien upon the title to and interest in real property and chattels real of the person against whom the warrant is issued in the same manner as a judgment duly docketed in the office of such clerk. The sheriff shall then proceed upon the warrant in the same manner, and with like effect, as that provided by law in respect to executions issued against property upon judgments of a court of record, and for services in executing the warrant he shall be entitled to the same fees, which he may collect in the same manner. In the discretion of the comptroller a warrant of like terms, force and effect may be issued and directed to any officer or employee of the department of finance, and in the execution thereof such officer or employee shall have all the powers conferred by law upon sheriffs, but he shall be entitled to no fee or compensation in excess of the actual expenses paid in the performance of such duty. If a warrant is returned not satisfied in full, the comptroller may from time to time issue new warrants and shall also have the same remedies to enforce the amount due thereunder as if the city of New York had recovered judgment therefor and execution thereon had been returned unsatisfied."

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